

AR64

1999 • ANNUAL • REPORT

# Primex





**P** RIMEX FOREST PRODUCTS LTD. is a Canadian company dedicated to the production and marketing of high quality lumber products from British Columbia's coastal forests. The Company which began in 1963 now has the following major operations and investments:

- ACORN FOREST PRODUCTS DIVISION, Delta, B.C. specializes in Hemlock structural and finishing components for traditional Japanese houses.
- SPECIALTY PRODUCTS DIVISION, Delta, B.C. is a kiln drying and lumber remanufacturing plant which produces value-added products for the U.S., Japanese and European markets.
- FIELD SAWMILLS LIMITED PARTNERSHIP, Courtenay, B.C. produces high value lumber products for the Japanese market.
- B. W. CREATIVE WOOD INDUSTRIES LTD., Maple Ridge, B.C. is owned 49% by Primex and 51% by B.W. Creative's management. The Company is one of Canada's leading producers of wooden spindles, stair parts and other specialty products.

Raw material for the sawmills is purchased competitively in the open market and Primex draws on many years of experience in the procurement of a suitable log supply. Primex continues at the forefront in sawmill technology with the objective of recovering the highest possible value from B.C.'s unique timber resource. Great pride is taken in the strong international customer base, which has been developed since 1973, for the Company's lumber products.

Primex Forest Products Ltd. is a publicly owned company with its shares listed on the Toronto Stock Exchange.

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# FIVE YEAR FINANCIAL HIGHLIGHTS

(in thousands of dollars, except per share amounts)\*

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	1999	1998	1997	1996	1995
Sales	197,781	168,079	155,784	170,672	160,461
Operating income	29,173	14,462	6,511	9,228	7,907
Depreciation	5,630	4,492	4,104	3,902	3,899
Interest	(728)	(263)	(34)	365	28
Earnings before income taxes	24,271	10,233	2,441	4,961	3,980
Income taxes	8,980	3,786	902	1,490	515
Net earnings	15,291	6,447	1,539	3,471	3,465
PER SHARE					
Pre tax earnings	1.44	0.59	0.14	0.28	0.23
After tax earnings	0.90	0.37	0.09	0.20	0.20
Cash flow from operations	1.77	0.85	0.38	0.51	0.46
Shareholders' equity	4.55	3.75	3.48	3.47	3.35
Dividends	0.08	0.08	0.08	0.08	0.13
Share price range:					
- high	6.45	3.75	4.53	4.88	5.38
- low	3.00	2.75	1.50	3.13	2.94
Average number of shares outstanding	16,904,987	17,387,270	17,381,328	17,381,328	17,381,328
YEAR END POSITION					
Working capital	50,893	47,245	41,680	36,388	34,651
Capital expenditures	4,264	2,282	2,117	3,814	3,099
Long term debt	848	7,716	6,071	1,032	1,301
Shareholders' equity	76,517	65,712	60,437	60,289	58,209
Number of shares outstanding	16,829,028	17,515,328	17,381,328	17,381,328	17,381,328

\* All numbers reflect a 2 for 1 share subdivision effective October 1999.



**A**t a Special General Meeting held September 15, 1999, Primex Forest Products Ltd.'s shareholders approved a two for one subdivision of the Company's common shares which was effective October 1, 1999. **All per share numbers in this report have been restated to reflect the two for one subdivision.**

For the year ended December 31, 1999 Primex Forest Products Ltd., Delta, B.C. had net earnings of \$15,291,000 or \$.90 per share compared to \$6,447,000 or \$.37 per share for the same period in 1998. Sales for 1999 were \$197,781,000 compared to \$168,079,000 in 1998. The significant increase in earnings was due to higher production and sales volumes combined with higher mill net lumber selling prices.

The Company had net earnings of \$5,227,000 or \$.30 per share for the fourth quarter of 1999 compared to \$3,664,000 or \$.21 per share for the same period in 1998. Sales for the fourth quarter of 1999 were \$51,475,000 compared to \$50,313,000 in 1998. The capital expenditure program previously announced for Field Sawmills led to costs totalling \$1,616,000 being expensed during the fourth quarter of 1999. These costs include writing down fixed assets and providing for employee severance, early retirement and relocation.

Expensing these costs reduced after tax earnings by \$.06 per share.

Working capital was \$50,893,000 at December 31, 1999 compared to \$47,245,000 at December 31, 1998. Shareholders' equity increased to \$76,517,000 at December 31, 1999 from \$65,712,000 at December 31, 1998. The net long-term debt to shareholders' equity ratio was .01 to 1.00 at December 31, 1999 compared to .12 to 1.00 at December 31, 1998.

A total of \$1,353,000 or \$.08 per share was paid in dividends in 1999. The Board of Directors declared a regular quarterly dividend of \$.02 per share on the common shares of the Company payable February 15, 2000 to shareholders of record February 8, 2000. In addition, the Board declared an extraordinary dividend of \$.10 per share on the common shares of the Company also payable February 15, 2000 to shareholders of record on February 8, 2000 due to the Company's record net earnings in 1999 and very strong financial position.

Capital expenditures during 1999 totalled \$4,264,000 for replacement of mobile equipment and sawmill improvements, including the start of two projects at Field Sawmills: a new log processing line which was completed in January 2000 and an automated lumber sorting system expected



to be completed by June 2000. These projects will give Field an expanded product line, greater flexibility and lower unit costs. The cost to complete these projects, estimated at \$8,000,000, will be financed from cash flow in the current year.

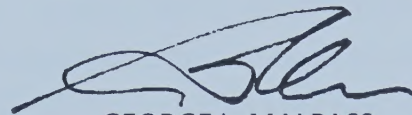
The Company continued to purchase common shares under its normal course issuer bid and purchased a total of 686,300 common shares at a cost of \$2,493,000 during 1999. The Company renewed its normal course issuer bid in October 1999 and is continuing to purchase shares in 2000. The total common shares issued and outstanding as at December 31, 1999 was 16,829,028.

During 1999 the Acorn, Field and Specialty Products operations received "Chain of Custody Certification" for product derived from Forest Stewardship Council endorsed forest operations.

Housing starts in Japan improved only slightly in 1999 over 1998 and the forecast for 2000 is similar to 1999. Therefore, it is expected that lumber consumption and demand will remain stable in 2000. While oversupply remains a concern, as it could push prices lower, the major factor affecting price levels is expected to be currency exchange rates. The cost of open market logs is expected to remain stable

during the first half of the year while the selling price of residual wood chips, which is tied to the price of market pulp, should continue to increase.

Respectfully submitted  
on behalf of the Board.



GEORGE L. MALPASS

President & Chief Executive Officer

March 2000



**INCORPORATION**

The Company was incorporated on May 27, 1963 under the laws of the Province of British Columbia by Memorandum and Articles under the name Evergreen Studs Limited. The Company changed its name to Acorn Forest Products Ltd. in November 1963, to Gregory Manufacturing Limited in April 1972 and finally to Primex Forest Products Ltd. in May 1986.

Field Sawmills Limited Partnership was established January 1, 1992, with Primex owning 70% and MacMillan Bloedel Limited owning 30%. Effective October 1, 1998, Primex purchased MacMillan Bloedel Limited's 30% interest, bringing Primex's ownership to 100%.

The Company has two wholly owned subsidiaries, Primex Fibre Ltd. and Primex Log Trading Ltd. Primex Fibre Ltd. owns a pulp chip manufacturing facility. This facility chips residual wood from the Acorn Forest Products Division and provides fee for service whole log custom chipping. Primex Log Trading Ltd. procures log supply for the sawmills.

The Company's principal office is located at 9924 River Road, Delta, B.C. V4G 1B5 and its registered office is located at #1300 - 777 Dunsmuir Street, Vancouver, B.C. V7X 1K2.

In this document, a reference to the "Company" or "Primex" means Primex Forest Products Ltd. and its predecessors and all of its subsidiaries.

**NARRATIVE DESCRIPTION OF THE BUSINESS**

Primex's principal business is the manufacture and marketing of high value lumber products for the Japanese market. The Company's operations and investments include:

- Acorn Forest Products Division (Acorn)
- Field Sawmills Limited Partnership (Field)
- Specialty Products Division (Specialty)
- Timber Division (Timber)
- B.W. Creative Wood Industries Ltd. (B.W. Creative)

**Acorn**

The Acorn operation, located on the Fraser River in Delta, British Columbia, consists of a log dewatering and merchandising system, a sawmill and a planermill. The log dewatering and merchandising system was constructed in 1988. The sawmill was completely rebuilt in 1989 after a fire that destroyed substantially all sawmilling equipment.

Acorn specializes in the sizes and grades of lumber components used in Japanese traditional housing. Species cut include hemlock, Douglas fir and spruce. Logs are sourced through log/wood chip trades and open market purchases. Sawmill production in 1999 was 163 million feet. Acorn had 220 employees at the end of 1999.



### **Field**

The Field operation, located in Courtenay, British Columbia, consists of a sawmill, in-line planer and planermill. The sawmill has undergone significant capital improvement over the last few years, adding new breakdown, edging and planer capacity.

Field specializes in the sizes and grades of lumber components used in Japanese traditional housing. Species cut include hemlock, Douglas fir, spruce and cypress. Logs are sourced through log/wood chip trades and open market purchases. Sawmill production in 1999 was 96 million feet. Field had 219 employees at the end of 1999.

### **Specialty**

The Specialty operation, located in Delta, British Columbia, consists of dry kilns and lumber remanufacturing equipment. The facility produces value-added products for the U.S., Japanese and European markets. Specialty had 34 employees at the end of 1999.

### **Timber**

The Timber Division manages timber sales under the British Columbia government's Small Business Forest Enterprise Program. During 1999 31,000 cubic meters of logs were harvested from these timber sales.

### **B.W. Creative**

Primex owns 49% of B.W. Creative, located in Maple Ridge, British Columbia, which manufactures and markets wooden spindles, stair parts and other specialty products. Its major markets are the U.S., United Kingdom and Canada.

Although Primex has over 200 customers throughout Japan, most sales are made through the large Japanese trading companies which provide services such as trade financing to the end customers. The four largest of these trading companies accounted for in aggregate 56% of the Company's total sales during the year.



# 1 COMPARISON OF 1999 & 1998 OPERATING RESULTS

	1999	1998
Sales	\$ 197,781,000	\$ 168,079,000
Net Earnings	\$ 15,291,000	\$ 6,447,000
Net Earnings Per Share	\$ .90	\$ .37

The earnings at the Acorn Forest Products Division (Acorn) and the Field Sawmills Limited Partnership (Field) vary according to lumber selling prices, currency exchange rates, ocean freight costs, log costs, by-product revenues, production volumes and operating costs.

Total sales in 1999 were 72% Japan, 6% Canada, 17% United States and 5% Europe and other offshore. In 1998 total sales were 73% Japan, 7% Canada, 13% United States and 7% Europe and other offshore. Canadian sales include outside log sales from our managed timber licences and fee for service charges at the Specialty Products Division (Specialty). Sales to Japan and the United States are denominated in U.S. dollars and, therefore, the U.S./Canadian exchange rate has an impact on earnings. On average for the year \$1.00 U.S. bought \$1.4857 Cdn. in 1999 versus \$1.4681 Cdn. in 1998, a favourable change of 1% for Primex.

Ocean freight costs, on a per unit shipped basis, were down by approximately 7.1% in Canadian dollars during 1999 from 1998.

Average lumber selling prices in Canadian dollars increased in 1999 by 4% from 1998.

During 1999, Primex sourced 99% of its log requirements on the open market or through chip/log trade agreements, all at market prices.

The balance was provided by managed timber sale licences. Open market log costs fluctuated during the year, but on average they were lower than 1998 by 1%.

Primex accounts for its by-product revenue, mainly from wood chips, as a reduction of gross log cost in calculating the cost of lumber produced. Therefore, while changes in by-product revenue do not affect reported sales, they can have a significant impact on margins and, hence, earnings. Revenue from wood chips, on a per unit basis, was 6.2% less than in 1998.

Acorn lost four production days in 1999 due to log shortages compared to 17 days lost in 1998 due to lack of demand for lumber in the Japanese market. Total production volume increased to 163 million board feet from 156 million in 1998 while per unit manufacturing costs increased by 8.8%.

Field lost no production days in either 1999 or 1998. Total production was 96 million board feet in 1999 up from 93 million board feet in 1998. Per unit manufacturing costs in 1999 were 3.9% higher than 1998.

Specialty operates on a "fee for service" basis providing kiln drying and lumber remanufacturing services for our own mills and several outside customers. Its earnings, therefore, are related to volume of throughput and operating costs. This division suffered a small loss in both 1999 and 1998.

B.W. Creative Wood Industries Ltd. (B.W. Creative), owned 49% by Primex, contributed to earnings in 1999 which is reflected in the accompanying financial statements by the proportionate consolidation method.



## 2 CAPITAL EXPENDITURES

Year	Description	Total
1998	Sawmill improvements, replacement of mobile equipment and plant improvements at B.W. Creative Wood Industries Ltd.	\$2,282,000
1999	Sawmill improvements including extensive log bucking modifications at Field Sawmills and replacement of mobile equipment.	\$4,264,000
2000	Sawmill improvements including installation of a J-Bar sorter system at Field Sawmills and replacement of mobile equipment approved by the Board of Directors to February 29, 2000.	\$10,455,000

## 3 FINANCIAL POSITION

During 1999 the Company generated \$21,717,000 from operations. Net additions in non-cash working capital balances from the levels of the previous year, mainly increased log inventories, consumed cash of \$11,997,000. The Company used \$4,264,000 to purchase fixed assets, \$7,683,000 to reduce long term debt and \$1,353,000 was paid as dividends. During the year the Company also used \$2,493,000 to repurchase common shares under its normal course issuer bid and \$640,000 to acquire outstanding stock options.

Along with the proceeds on disposition of fixed assets of \$119,000, this resulted in a decrease in cash of \$6,594,000 for the year and cash on hand of \$12,704,000 at December 31, 1999.

During the year the Company paid off the long term debt associated with Field Sawmills in the amount of \$7,400,000. The balance of term debt shown on the balance sheet in the

amount of \$848,000 is primarily the Company's share of the term debt of B.W. Creative Wood Industries Ltd. The Company had unused operating lines of credit totalling \$25,000,000 available at year end.

At a Special General Meeting held September 15, 1999, the Company's shareholders approved a two for one subdivision of the Company's common shares which was effective October 1, 1999. All the per share numbers in this report reflect the two for one subdivision.

During the year the Company purchased 686,300 common shares at a cost of \$2,493,000 under its normal course issuer bid. The Company renewed its normal course issuer bid in October 1999 and is continuing to purchase common shares in 2000. The total common shares issued and outstanding at the end of 1999 was 16,829,028.

Shareholders' equity increased to \$76,517,000 or \$4.55 per share at December 31, 1999 from \$65,712,000 or \$3.75 per share at December 31, 1998.

## 4 LIQUIDITY

At December 31, 1999, the Company had net cash on hand of \$12,704,000. The Company's working capital was \$50,893,000 at December 31, 1999 compared to \$47,245,000 at December 31, 1998. The current ratio was 3.38 to 1.00 at December 31, 1999, compared to 3.89 to 1.00 at December 31, 1998. The net long term debt to equity ratio was .01 to 1.00 at December 31, 1999 compared to .12 to 1.00 at December 31, 1998. The capital expenditures completed during 1999 were financed from cash flow and the capital expenditures approved to February 29, 2000 will also be financed from cash flow.



## 5 RISKS, UNCERTAINTIES, SENSITIVITIES

### (a) Japanese Market Concentration

In 1999 72% of the Company's sales were to Japan. Demand for lumber in the Japanese market fell sharply during 1997 and 1998 as housing starts in 1998 were down 27% from the peak in 1996 resulting in significantly lower lumber consumption. Demand and consumption stabilized in 1999 at virtually the same levels as 1998 and are expected to remain at those levels in 2000. Changes in Japanese house building codes and mandatory warranties beginning in June 2000 will have an effect on demand for various types of lumber products. Despite these changes management believes that Japan will continue to be our most important market and that the Company is well positioned to meet the changing demands.

### (b) Log Supply

The Company's sources of log supply in 1999 were: timber sale licences 1%; wood chip/log trade agreements 29%; and, open market purchases 70%. Logs acquired under chip/log agreements are priced at market.

Prices and availability of logs in the open market are affected by supply and demand factors. The major factors impacting log availability in coastal B.C. are the high logging cost structure on Crown lands and over capacity in the manufacturing sector. Until the overcapacity situation is rectified, sourcing logs suitable for the Company's mills will continue to be a challenge.

### (c) Currency Exchange Rates

Primex sells to the Japanese and United States markets in U.S. dollars. In 1999, sales to these markets amounted to 89% of total sales. It is expected that sales to these markets will amount to approximately that percentage in 2000. Based on projected sales volumes for 2000, a \$.01 change in the Canadian dollar versus the U.S. dollar at current rates would affect net earnings for that year by approximately \$1,350,000 or \$.08/share. In order to minimize foreign currency exchange rate volatility, the Company at opportune intervals will enter into forward exchange contracts hedging future U.S. dollar denominated sales and receivables. During 1999 the Company hedged \$16,650,000 U.S. at an average exchange rate of 1.4855. At December 31, 1999 the Company had outstanding forward exchange contracts totalling \$4,000,000 U.S. at an average exchange rate of 1.4752.

### (d) Environmental Constraints/Requirements

The Company has outside consultants monitor its operations on an on-going basis to ensure that the principles outlined in the Company's environment policy are being followed. As well as assessing compliance with existing environmental regulations, the consultants recommend improvements in standards. Projects to improve standards are undertaken as recommended. Based on the consultants' reports, the Board of Directors believes that the Company is in substantial compliance with existing environmental laws.

During 1999 Acorn, Field and Specialty operations received "Chain of Custody Certification" for product derived from Forest Stewardship Council endorsed forest operations.



#### **(e) Softwood Lumber Agreement**

On February 16, 1996 an agreement was reached between Canada and the United States of America designed to prevent the U.S. government and forest industry from initiating a countervailing duty investigation of Canadian softwood lumber exports to the U.S. for the next five years.

As a result of the agreement individual Canadian companies were assigned a quota for free access to the U.S. softwood lumber market, with shipments beyond that subject to fees, currently of \$52.93 U.S. per thousand board feet on a small specified volume and \$146.25 U.S. per thousand board feet on shipments in excess of that for companies in British Columbia.

The U.S. accounted for 21% by volume (17% by value) of Primex's total sales in 1999. The fourth year of the quota system expires March 31, 2000 and it appears that Primex will be subject to payment of fees for shipments in excess of the quota. Three quarters of the estimate of fees payable have been provided for in the 1999 financial statements based on a pro-rata assignment of the fees for the year.

The agreement restricts Primex's ability to increase sales to the U.S. without paying a penalty, which limits Primex's ability to react to changing market conditions.

#### **(f) Union Agreement**

The Company's hourly employees are members of I.W.A. Canada whose current Master Agreement will expire June 14, 2000. Industry negotiations are scheduled to begin in April. It is too early in the process to predict whether an agreement can be reached without disruptions.

## **6 OUTLOOK**

Housing starts in Japan improved only slightly in 1999 over 1998 and the forecast for 2000 is similar to 1999. Therefore, it is expected that lumber consumption and demand will remain stable in 2000. While oversupply remains a concern, as it could push prices lower, the major factor affecting price levels is expected to be currency exchange rates. The cost of open market logs is expected to remain stable during the first half of the year while the selling price of residual wood chips, which is tied to the price of market pulp, should continue to increase.



Primex Forest Products Ltd. will conduct all of its operations in a manner that promotes environmental sustainability and minimizes the potential for negative impacts on the environment. This principle of continued environmental protection and improvement will be achieved within the framework of regulatory compliance and operation as an efficient and profitable provider of quality forest products.

#### STATEMENT OF SENIOR MANAGEMENT SUPPORT

Primex's senior management supports and encourages the creation of a corporate Environmental Management System (EMS) to ensure and demonstrate compliance with our stated Guiding Principles and Policy Goals.

Senior management appreciates that development and implementation of an EMS will place additional demands on personnel and resources. They are, however, prepared to make the resources available as they recognize that these will be offset through increased environmental protection, and regulatory compliance, along with reduced liability, waste generation and subsequent treatment costs.

Management also recognizes that only through continued efforts to sustain and improve environmental quality can Primex's continued survival and growth be assured,

and that only through continued profitable operation can Primex allocate the resources necessary to achieve their environmental goals and objectives.

#### ORGANIZATION AND RESPONSIBILITIES

A management and organizational structure has been set up to define and document the responsibility, authority and interactions of key personnel who manage, perform and verify work affecting the environment.

A management structure includes representatives with organizational freedom and authority to:

- provide sufficient resources and personnel for implementation,
- initiate action to assure compliance,
- identify and record any environmental problems,
- initiate, recommend or provide solutions to those problems through designated channels,
- verify the implementation of such solutions,
- control further activities until any environmental deficiency or unsatisfactory condition has been corrected, and
- act in emergency situations.



The consolidated financial statements of Primex Forest Products Ltd. have been prepared by management in accordance with generally accepted accounting principles in Canada. The financial information contained elsewhere in the annual report is consistent with the consolidated financial statements.

Management maintains a system of internal controls over financial reporting which encompasses policies, procedures and controls to provide reasonable assurance that assets are safeguarded against loss or unauthorized use, that transactions are executed and recorded in accordance with management's authorization and that financial records are accurate and reliable.

The Audit Committee, which is comprised of a majority of outside directors, meets periodically with management and the external auditors to review the adequacy of the system of internal controls and the integrity of the Company's financial reporting.

## MANAGEMENT'S RESPONSIBILITY

The consolidated financial statements have been reviewed by the Audit Committee prior to submission to the Board. In addition, the consolidated financial statements have been audited by PricewaterhouseCoopers LLP, Chartered Accountants, who have full access to the Audit Committee with and without the presence of management. Their report follows.



G.L. Malpass  
President & Chief Executive Officer



P.D. Rivers  
Vice President - Finance  
Chief Financial Officer

February 18, 2000

## AUDITORS' REPORT

February 18, 2000

To the Shareholders of Primex Forest Products Ltd.

We have audited the consolidated balance sheets of Primex Forest Products Ltd. as at December 31, 1999 and 1998 and the consolidated statements of earnings and earnings reinvested in the business and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence

supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1999 and 1998 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.



Chartered Accountants  
Vancouver, B.C., Canada



# CONSOLIDATED STATEMENTS OF EARNINGS

AND EARNINGS REINVESTED IN THE BUSINESS  
FOR THE YEARS ENDED DECEMBER 31, 1999 AND 1998  
(in thousands of dollars)

	1999 \$	1998 \$
Sales and other income (note 6)	197,781	168,079
Expenses		
Cost of sales	144,549	129,936
Ocean freight	17,739	17,971
Selling and administration	6,358	5,718
Depreciation and amortization	5,630	4,492
Interest on long-term debt	106	289
Gain on disposal of fixed assets	(38)	(8)
Interest income	(834)	(552)
	173,510	157,846
Earnings before income taxes	24,271	10,233
Provision for income taxes (note 7)		
Current	8,146	2,267
Deferred	834	1,519
	8,980	3,786
Net earnings for the year	15,291	6,447
Earnings reinvested in the business – Beginning of year	61,581	56,743
Dividends paid (\$0.08 per share (1998 – \$0.08))	(1,353)	(1,391)
Stock options surrendered	(640)	–
Share purchase and cancellation (note 5)	(2,331)	(218)
Earnings reinvested in the business – End of year	72,548	61,581
Basic earnings per share (note 5)	0.90	0.37



# CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 1999 AND 1998

(in thousands of dollars)

	1999 \$	1998 \$
<b>Cash flows from operating activities</b>		
Net earnings for the year	15,291	6,447
Items not affecting cash		
Depreciation and amortization	5,630	4,492
Gain on disposal of fixed assets	(38)	(8)
Deferred income taxes	834	1,519
	21,717	12,450
Changes in non-cash working capital		
Accounts receivable	789	(2,981)
Inventories	(16,029)	6,016
Other	(8)	8
Accounts payable and accrued liabilities	(1,282)	2,165
Income taxes payable	4,533	1,034
	9,720	18,692
<b>Cash flows from financing activities</b>		
Proceeds of long-term debt	—	441
Repayment of long-term debt	(7,683)	(1,128)
Proceeds from sale of common shares	—	450
Stock options surrendered	(640)	—
Repurchase of common shares	(2,493)	(232)
Dividends paid	(1,353)	(1,391)
	(12,169)	(1,860)
<b>Cash flows from investing activities</b>		
Purchase of property, plant and equipment	(4,264)	(2,282)
Proceeds on disposition of fixed assets	119	196
Acquisition of interest in Field Sawmills Limited Partnership (note 2)	—	(3,261)
	(4,145)	(5,347)
<b>(Decrease) increase in cash</b>	<b>(6,594)</b>	<b>11,485</b>
<b>Cash – Beginning of year</b>	<b>19,298</b>	<b>7,813</b>
<b>Cash – End of year</b>	<b>12,704</b>	<b>19,298</b>
<b>Supplemental cash flow information</b>		
Interest received	755	552
Interest paid	106	289
Taxes paid	3,682	1,803



# CONSOLIDATED BALANCE SHEETS

AS AT DECEMBER 31, 1999 AND 1998

(in thousands of dollars)

	1999 \$	1998 \$
<b>ASSETS</b>		
<b>Current assets</b>		
Cash	<b>12,704</b>	19,298
Accounts receivable	<b>17,950</b>	18,739
Inventories (note 3)	<b>41,274</b>	25,245
Other	<b>310</b>	303
	<b>72,238</b>	63,585
<b>Property, plant and equipment</b>		
Equipment	<b>62,360</b>	58,901
Buildings	<b>10,642</b>	10,051
Leasehold improvements	<b>1,951</b>	1,947
	<b>74,953</b>	70,899
Less: Accumulated depreciation	<b>41,617</b>	36,305
	<b>33,336</b>	34,594
Land	<b>874</b>	874
	<b>34,210</b>	35,468
	<b>106,448</b>	99,053



**CONSOLIDATED BALANCE SHEETS**

AS AT DECEMBER 31, 1999 AND 1998

(in thousands of dollars)

	1999 \$	1998 \$
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities	12,772	13,866
Income taxes payable	5,244	711
Long-term debt due within one year (note 4)	110	925
Deferred income taxes	3,219	838
	21,345	16,340
<b>Long-term debt (note 4)</b>	848	7,716
<b>Deferred income taxes</b>	7,738	9,285
	29,931	33,341

**SHAREHOLDERS' EQUITY****Capital stock (note 5)**

Authorized

200,000,000 common shares of no par value

Issued

16,829,028 shares (1998 – 17,515,238 shares)

**Earnings reinvested in the business**

3,969	4,131
72,548	61,581
76,517	65,712
106,448	99,053

**Commitments (note 9)**

Approved by the Board

Director



Director





## 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Principles of consolidation

The consolidated financial statements include the accounts of Primex Forest Products Ltd., its wholly-owned subsidiaries and Field Sawmills Limited Partnership. B.W. Creative Wood Industries Ltd., a 49% indirectly owned joint venture, is accounted for by the proportionate consolidation method (together, the "Company").

All material intercompany transactions have been eliminated.

### Inventories

Cost is determined on the first-in, first-out (FIFO) basis. The inventories are valued as follows:

Logs	lower of cost and replacement cost
Lumber	lower of cost and estimated net realizable value
Chips and sawdust	net realizable value
Operating supplies	cost

### Logging development costs

Logging development costs are being amortized on a unit-of-production basis, based on estimated total logging costs and log production, by area, within the Company's timber licences.

### Property, plant and equipment

Property, plant and equipment are stated at cost. The costs of repairs and replacements of a routine nature are charged to earnings while those expenditures which improve or extend the useful lives of the assets are capitalized.

Depreciation is provided using the straight-line method at rates sufficient to amortize the costs over the estimated useful lives of the assets as follows:

Buildings and yard	20 to 40 years
Plant equipment	10 to 15 years
Mobile equipment	3 to 5 years
Other	2 to 5 years
Leasehold improvements	over the lease term

### Derivative financial instruments

Derivative financial instruments in the form of foreign exchange contracts are utilized to hedge certain transactions denominated in foreign currencies, primarily export sales. These instruments serve to protect the Company from currency fluctuations between the transaction date and settlement. The Company does not hold or issue financial instruments for trading purposes.

### Foreign currency translation

Accounts receivable that are hedged by forward exchange contracts are translated at the forward exchange contract rates. Other amounts receivable and payable in foreign currencies are translated to Canadian dollars at the year-end rate of exchange. Revenue and expenses not hedged are translated throughout the year at the prevailing exchange rates. All exchange gains and losses are included in the determination of net earnings for the year.

### Use of estimates

The preparation of the consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.



# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 1999 AND 1998

(tabular amounts in thousands of dollars)

## 2 ACQUISITION

Effective October 1, 1998, the Company acquired the 30% interest in Field Sawmills Limited Partnership (Field) not already owned. As a result, Field is now wholly-owned and has been fully consolidated from the date of purchase. Previously, it was proportionately consolidated. The purchase price was allocated based on fair values as follows:

	<b>\$</b>
Net assets acquired	
Current assets – net	2,428
Property, plant and equipment	3,159
	<hr/>
	5,587
Less: Long-term debt	2,326
	<hr/>
Cash consideration	3,261
	<hr/>

## 3 INVENTORIES

	1999	1998
	\$	\$
Logs	31,562	16,003
Lumber	9,326	8,908
Chips	28	66
Operating supplies	358	268
	<hr/>	<hr/>
	41,274	25,245
	<hr/>	<hr/>

## 4 LONG-TERM DEBT

	1999	1998
	\$	\$
Floating rate term bank loan, repaid in 1999	–	7,400
Other	958	1,241
	<hr/>	<hr/>
	958	8,641
Less: Amounts due and repayable in one year	110	925
	<hr/>	<hr/>
	848	7,716
	<hr/>	<hr/>

Annual payments of principal required to meet debt obligations are as follows:

	\$
2000	110
2001	104
2002	112
2003	131
2004	11
Thereafter	490
	<hr/>
	958
	<hr/>



## 5 CAPITAL STOCK

At a Special General Meeting on September 15, 1999, shareholders approved a two for one subdivision of the Company's common shares and an increase in authorized common shares to 200,000,000 effective October 1, 1999. All per share numbers in the accompanying statements have been restated to reflect the two for one subdivision.

Pursuant to a normal course issuer bid the Company, on a pre-split basis, acquired and cancelled 342,600 common shares (1998 – 33,000 shares). On a post-split basis, the company acquired and cancelled 1,100 shares. The total purchase consideration was \$2,493,000, of which \$162,000 has been deducted from share capital and \$2,331,000 has been deducted from earnings reinvested in the business.

In 1999, the Company amended its Stock Option Plan to permit the tendering of stock options for cash. During the year, optionees tendered 260,000 shares (on a post-split basis) for \$1,040,000. The cost has been charged to earnings reinvested in the business, net of applicable income taxes of \$400,000.

A stock option for 100,000 common shares (on a pre-split basis) was exercised in 1998. The proceeds of \$450,000 was added to share capital.

The following stock options, granted to directors and key employees under the Company's executive stock option plan, are outstanding as at December 31, 1999:

Year of grant	Number of shares	Price \$	Exercise period	Expiry date
1992	700,000	2.25	1997–2002	Mar. 11, 2002
1995	4,000	4.375	2000–2005	Jul. 18, 2005
1996	4,000	3.875	2001–2006	Mar. 1, 2006
1997	44,000	3.725	2002–2007	Jul. 25, 2007
1998	86,000	3.425	2003–2008	Jan. 29, 2008
1999	6,000	3.625	2004–2009	Jan. 28, 2009

Fully diluted earnings per share, which have been calculated on the basis that all stock options were exercised on the date of grant notwithstanding their earliest exercise date, were \$0.86 per share for the year ended December 31, 1999, based on 17,748,987 net shares outstanding during the year (\$0.35 per share for 1998 based on 18,485,270 net shares for that year). Basic earnings per share calculations have been based on 16,904,987 (1998 – 17,387,270) weighted average net outstanding shares during the year.

## 6 SEGMENTED INFORMATION

The Company's operating segments for reporting purposes are based on a products and services orientation. Purchases and sales of goods and services between operating segments are made at the Company's best estimates of fair values at the time of the transactions. The operating segments are:

Solid Wood – Acorn Forest Products Division, Field Sawmills Limited Partnership and Timber Division.

Other – Specialty Products Division and B.W. Creative Wood Industries Ltd.



# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 1999 AND 1998  
(tabular amounts in thousands of dollars)

	Year ended December 31, 1999			
	Solid Wood \$	Other \$	Consolidation adjustments \$	Total 1999 \$
Sales and other income				
External	183,423	14,358	—	197,781
Internal	553	2,770	(3,323)	—
	183,976	17,128	(3,323)	197,781
Cost and expenses	156,371	15,560	(3,323)	168,608
Interest income	(855)	—	—	(855)
Interest expense	29	98	—	127
Depreciation	5,240	390	—	5,630
	160,785	16,048	(3,323)	173,510
Earnings before income taxes	23,191	1,080	—	24,271
Provision for income taxes	—	—	8,980	8,980
Net earnings for the year	23,191	1,080	(8,980)	15,291
Capital expenditures	3,958	306	—	4,264
Total assets at year end	98,944	7,504	—	106,448

	Year ended December 31, 1998			
	Solid Wood \$	Other \$	Consolidation adjustments \$	Total 1998 \$
Sales and other income				
External	157,010	11,069	–	168,079
Internal	771	–	(771)	–
	157,781	11,069	(771)	168,079
Cost and expenses	143,751	10,637	(771)	153,617
Interest income	(593)	–	–	(593)
Interest expense	214	116	–	330
Depreciation	4,133	359	–	4,492
	147,505	11,112	(771)	157,846
Earnings before income taxes	10,276	(43)	–	10,233
Provision for income taxes	–	–	3,786	3,786
Net earnings for the year	10,276	(43)	(3,786)	6,447
Capital expenditures	1,675	607	–	2,282
Total assets at year end	92,639	6,414	–	99,053



Sales and other income by location of customer are as follows:

	1999 \$	1998 \$
Japan	141,510	122,469
Canada	12,865	12,793
United States	32,677	21,028
Europe and other	10,729	11,789
	<b>197,781</b>	168,079

## 7 INCOME TAXES

The effective tax rate of the Company for the years ended December 31, 1999 and 1998 differed from the combined federal and provincial statutory rates as follows:

	1999 %	1998 %
Combined federal and provincial statutory rate	45.6	45.6
Manufacturing and processing allowance	(7.0)	(7.0)
Subtotal	38.6	38.6
Other	(1.6)	(1.6)
	<b>37.0</b>	37.0

## 8 FINANCIAL INSTRUMENTS

### Credit risk

Although the majority of the Company's lumber sales are to the Japanese market, the credit risk arising from concentration in this market is minimized as lumber sales are realized from a number of large customers and are generally secured by letters of credit or equivalent instruments of guarantee. The Company deals only with highly rated financial institutions for these instruments. Log sales, mainly to the domestic market, are generally transacted on a cash basis. As a result, the Company is not exposed to significant risk of credit-related losses.

### Foreign exchange risk

The majority of the Company's lumber sales are denominated in U.S. dollars. The Company is exposed to risk of loss depending on the relative movement of this currency against the Canadian dollar. Exposure to foreign exchange fluctuations is managed through the use of forward exchange contracts.

At December 31, 1999, the Company had outstanding foreign exchange contracts in the amount of U.S.\$4,000,000 (1998 – \$nil) at an average rate of \$1.4752 to \$1 U.S. expiring in the first quarter of 2000.

### Long-term debt

The fair value of long-term debt approximates book value at December 31, 1999 and 1998.

### Current assets and liabilities

The carrying values reported in the balance sheet for cash, accounts receivable, and accounts payable and accrued liabilities are reasonable estimates of fair values.

## 9 COMMITMENTS

The Company is obligated under operating lease agreements for aggregate basic annual rentals of approximately:

	\$
2000	594
2001	546
2002	535
2003	378
2004	378

## 10 PENSION PLANS

The majority of the Company's salaried employees are eligible to participate in pension plans after one year of service. Required company contributions are based on a percentage of compensation and are charged to earnings as incurred. The majority of the Company's hourly paid workers are enrolled in a pension plan into which the Company pays a rate per hour worked. These payments are charged to earnings as incurred.

## 11 UNCERTAINTY DUE TO THE YEAR 2000 ISSUE

The Year 2000 Issue arises because many computerized systems use two digits rather than four digits to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using the year 2000 date is processed. In addition, similar problems may arise in some systems that use certain dates in 1999 to represent something other than a date. Although the change in date has occurred, it is not possible to conclude that all aspects of the Year 2000 Issue that may affect Primex, including those related to customers, suppliers, or other third parties, have been fully resolved.





Undergrowth of Second Growth Forest

## CORPORATE INFORMATION

**DIRECTORS**

LORNE R. BOLTON\*

Company Director

GEORGE L. MALPASS

President & Chief Executive Officer  
Primex Forest Products Ltd.

CONRAD A. PINETTE\*

President and Chief Operating Officer  
Lignum Ltd.

DONALD H. REED\*

Company Director

PAUL D. RIVERS\*

Vice President – Finance & Secretary  
Primex Forest Products Ltd.

JOHN P. SULLIVAN

Vice President – Corporate Development  
Primex Forest Products Ltd.

\* Members of the Audit Committee

**OFFICERS**

GEORGE L. MALPASS

President & Chief Executive Officer

PAUL D. RIVERS

Vice President – Finance & Secretary

JOHN P. SULLIVAN

Vice President – Corporate Development

JOHN N. BURCH

Vice President – Marketing

ED R. VERVYNCK

Vice President – Manufacturing

**REGISTRAR AND TRANSFER AGENT**

The Montreal Trust Company  
Vancouver, B.C., Toronto, Ontario

**SHARES LISTED**

The Toronto Stock Exchange – PXF

**BANKERS**

Royal Bank of Canada

**SOLICITORS**

McCarthy Tétrault, Vancouver, B.C.

**AUDITORS**

PricewaterhouseCoopers LLP, Vancouver, B.C.

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**ANNUAL MEETING**

Thursday April 27, 2000, 2:30 p.m.

The Four Seasons Hotel, Vancouver, B.C.

**OPERATIONS & INVESTMENTS**

- Acorn Forest Products Division, Delta, B.C.
- Specialty Products Division, Delta, B.C.
- Field Sawmills Limited Partnership, Courtenay, B.C.
- Timber Division, Courtenay, B.C.
- Primex Fibre Ltd., Delta, B.C.
- Primex Log Trading Ltd., Delta, B.C.
- B.W. Creative Wood Industries Ltd., Maple Ridge, B.C.





**PRIMEX**  
FOREST PRODUCTS LTD.